In the Supreme Court of the United States

OCTOBER TERM, 1971

No. 70-28

UNITED STATES OF AMERICA, PETITIONER

v.

EDNA GENERES, WIFE OF, AND ALLEN H. GENERES

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

Although the arguments advanced in respondent's brief are adequately dealt with in our opening brief, we file this reply to discuss and amplify a single point. This is prompted by respondent's assertion (Br. 22-24) that the government is inconsistent in urging application of the standard of dominant motivation in this case, while having urged in *United States* v. *Donruss Co.*, 393 U.S. 297, that a significant motivation to avoid individual income tax is sufficient to impose liability for the accumulated earn-

ings tax under Section 531 of the Internal Revenue Code.

In so contending, respondent misunderstands the function of Section 531 and this Court's opinion in *United States* v. *Donruss Co.*, *supra*, upon which he places major reliance. Section 531, as the Court observed in *Donruss* (393 U.S. at 303), "is one congressional attempt to deter use of a corporate entity to avoid personal income taxes." This congressional intent provides a sound reason for applying the standard of significant motivation, since the effect of its application is to deny the sought-after tax advantage whenever it appears that the transaction has been shaped or is affected to any substantial degree by the purpose to avoid individual income tax. Application of the dominant standard in that context would frustrate the prophylactic purpose of Section 531, in that it would encourage taxpayers to engage in the legislatively disapproved tax-avoidance activities in the hope of passing muster under that standard. See *United States* v. *Donruss Co.*, *supra* at 307-308.

It was in recognition of the appropriateness of the standard of significant motivation in the context of a prophylactic provision that the Court made it plain (*id.* at 308-309) that there is no universal standard of motivation to be applied under all sections of the Internal Revenue Code, and that each provision of the Code must be considered on its own bottom, by reference to its particular language, purpose, and legislative history. Indeed, in holding in *Donruss*

that the significant standard was appropriate in the accumulated earnings tax area, the Court rejected as inapposite a number of its own tax decisions in other areas in which the dominant standard had been applied.

Section 166 does not involve considerations similar to those that guide decision under Section 531. Its purpose, in contrast to that of Section 531, is not to discourage either the business or nonbusiness loans for which disparate tax treatments are prescribed. Each type of activity is equally acceptable, as active business and investment are equally acceptable. It is therefore necessary under this provision only to differentiate one from the other, since the Congress has provided one tax treatment for losses from investment or personal loans, and another for losses from business loans. *Whipple* v. *Commissioner*, 373 U.S. 193, 202. Only the dominant standard, consistently with these considerations, provides a neutral approach to the problem by requiring a comparison between the taxpayer's business interest and nonbusiness interest, and by resolving the ultimate issue on the basis of identification of the weightier. The significant standard, on the other hand, is not neutral in its application. It prevents classification by the trier of fact based upon meaningful differentiation between the taxpayer's business and nonbusiness interests.*

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* Respondent notes (Br. 21 n. 5) that the government has urged the significant standard in contemplation-of-death cases arising under Section 2035. Since the purpose of that provision, like the purpose of Section 531, is to remove an in-

It permits the perverse result of identifying the loss by its lesser component.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

SEPTEMBER 1971.

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centive for taxpayers to engage in tax-avoidance activity—*i.e.*, making *inter vivos* gifts as a substitute for testamentary dispositions—there is no inconsistency with our position here.

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